

No. 22443

In the
United States Court of Appeals
For the Ninth Circuit

ALLSTATE INSURANCE COMPANY, an Illinois
corporation,

Appellant,

vs.

NELSON CHRISTIAN DORR and AEDA DORR,
his wife, surviving parents of FELIX
MATTHEW DORR, deceased, et al,

Appellees.

Opening Brief of Appellant
Allstate Insurance Company

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SUBJECT INDEX

	Page
Jurisdiction	1
Statement of Case	2
Specification of Errors	5
Argument of the Case (Summary of Argument).....	6
Conclusion	13
Appendix	

TABLE OF AUTHORITIES

CASES	Pages
Allgeyer v. Louisiana, 165 U.S. 578.....	10
American National Ins. Co. v. Caldwell, 70 Ariz. 78, 216 P.2d 413	11
Atlantic Coastline v. Goldsboro, 232 U.S. 548.....	7
Byrnes v. Mutual Life Ins. Co., 217 F.2d 497.....	11, 13
Conold v. Stern, (Ohio) 35 N.E.2d 133.....	11, 13
Covington v. Sanford, 164 U.S. 592.....	8
Departments of Finaneial Institutions v. Holt, (Ind.) 108 N.E.2d 629	8, 12
First National Benefit Society v. Fisk, 55 Ariz. 290, 101 P.2d 205	11
Ill. Bankers' Life Assn. v. Theodore, 44 Ariz. 160, 34 P.2d 423	11
Jenkins v. Mayflower, 93 Ariz. 289, 380 P.2d 145.....	9
Liggett Co. v. Baldridge, 278 U.S. 105.....	7, 12
Modern Woodmen of America v. Stevens, 70 Ariz. 232, 219 P.2d 322	11
Mutual Life Ins. Co. of N. Y. v. Morairty, 178 F.2d 470.....	11
Phoenix Metals Corp. v. Roth, 79 Ariz. 106, 284 P.2d 645.....	7
Sandoval v. Chenoweth, 102 Ariz. 241, 428 P.2d 98.....	9, 10
Scheeter v. Killingsworth, 93 Ariz. 273, 380 P.2d 136.....	9, 12
Smith v. Texas, 233 U.S. 630.....	8
State Farm Mut. v. Butler, (Va.) 125 S.E.2d 823.....	13
Treigle v. Acme Homestead Assn., 279 U.S. 189.....	8
U. S. v. Seven Oaks Dairy Co., 10 F.Supp. 995 (D.C. Mass. 1935)	10

TABLE OF AUTHORITIES

iii

CASES	Pages
Valley National Bank of Phoenix v. Glover, 62 Ariz. 538, 159 P.2d 292	7
Wolff Packing Co. v. Court of Industrial Relations, 262 U.S. 522	11

CONSTITUTIONS

U. S. Constitution, 14th Amendment.....	6, 7, 8, 10
Constitution of the State of Arizona, Article II, Section 4.....	6, 7

STATUTE

28-1170 A.R.S.	5, 9
---------------------	------

TEXT

16 Am. Jur. 2d 706, Constitution of Law, Sec. 373.....	10
--	----

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Appellees.

Opening Brief of Appellant Allstate Insurance Company

JURISDICTION

This action originated in the United States District Court for the District of Arizona, jurisdiction being vested in the District Court by virtue of there being complete diversity of Citizenship between the parties and the amount in controversy exceeding \$10,000.00 exclusive of interest and costs. (Paragraph I, Amended Complaint, TR 1, 28 USCA § 1332.) By Motion dated May 9, 1967, the Defendants, Nelson Christian Dorr and Jane Doe Dorr, his wife, moved for summary judgment against the Plaintiff, Allstate Insurance Company, and Safeco Insurance Company of America, the Third Party Defendant (TR 14). Such motion was

granted against Plaintiff, Allstate, by order dated September 5, 1967 (TR 58) and judgment was entered thereupon dated September 11, 1967 (TR 59) which included the finding pursuant to Federal Rule of Procedure 54(d) permitting a partial judgment to be final. Thereafter, and within the time provided by law, the Plaintiff Allstate proceeded upon this appeal (TR 61).

STATEMENT OF THE CASE

For convenience, the parties will be referred to in an abbreviated but easily recognizable manner; i.e. Allstate, Mr. and Mrs. Dorr or Dorrs, Mrs. Gutierrez, Badger and Safeco.

This is a declaratory judgment action brought by Allstate against all other parties (except Safeco, who was brought in as a third party defendant by Mrs. Gutierrez) to determine that Allstate had no coverage under a policy issued by it naming Mrs. Gutierrez as the named insured. (Plaintiff's Amended Complaint, Paragraphs II and IV, TR 1, 5.)

The Defendant, Virginia Wathen Gutierrez, filed an application for insurance with the Plaintiff, Allstate, which bore the date of January 29, 1964. (See Affidavit of Vic Hooper dated May 24, 1967, to which is attached the application of Defendant Gutierrez, both supporting documents to the Supplemental Response of the Plaintiff to Motion for Summary Judgment. TR 38-40.) It is to be noted that immediately preceding the signature of the Defendant Gutierrez (wherein she signed Virginia A. Wathen), two statements were answered in the negative by the Defendant Gutierrez. The first question was:

“Has any insurer cancelled or refused or given notice that it intends to cancel or refuse any similar insurance?”

The second of such questions was:

“Has any license or permit to drive any automobile been revoked, suspended or refused?”

Both of such questions were answered in the negative by the applicant and as will hereafter be seen, both of such questions were in fact answered falsely.

In addition, the applicant, Mrs. Gutierrez, also included false information in her application by stating under paragraph 4 on the second page of the application that she had received one ticket for an illegal turn in the past five years prior to the making of the application (TR 40). As will be seen hereafter, such statement is likewise false.

In addition, the applicant, Mrs. Gutierrez, also stated under paragraph 5 of the second page of the application that the principal operator of the motor vehicle would be herself and that her driver's license number “will follow”. The applicant, the Defendant, Mrs. Gutierrez, also under paragraph 4 of the second page indicated that she would be the only person in the household who would be operating the motor vehicle (TR 40). All of these statements were false.

Attached to the Supplemental Response to Motion for Summary Judgment is the affidavit of Mildred R. Kunkel certifying that the Defendant, Mrs. Gutierrez, on October 16, 1963, failed the law portion of her driver's test and she was, therefore, refused a driver's license. In addition, also attached thereto and certified by the same individual is an abstract of driving record of the Defendant, Mrs. Gutierrez, establishing that in addition to the illegal turn ticket that Mrs. Gutierrez admitted receiving in 1963, she had also within the five years preceding the application received citations and fines for driving while under the influence of intoxicating beverages, reckless driving and running a red light (TR 57).

After the accident with which this lawsuit is concerned, a recorded statement was taken from the Defendant, Mrs. Gutierrez, and her son, Robert. A transcript of that statement was attached to the Supplemental Response to Motion for Summary Judgment (TR 42 to TR 53). In such transcript the Defendant, Mrs. Gutierrez (contrary to the indication in her application for insurance that she had a valid driver's license and would provide the license number) admitted that she had failed a written test for the driver's license in Arizona and had not since secured a driver's license (TR 42). In addition, (and again contrary to her application wherein she indicated she would be the only principal operator of the motor vehicle) she acknowledged by her silence the truth of the statement of her son Bob Wathen that after she failed the driver's license test, the automobile was driven only by either Lombardo or her son Robert or other friends (TR 49). Also in such transcript the Defendant, Mrs. Gutierrez, admitted that prior to the application for the policy of insurance with Allstate, she was refused a renewal of insurance by her previous agent (TR 50-51). In a later portion of the statement, in describing the transaction with that agent, she stated that policy of insurance had been cancelled (TR 52).

After the Plaintiff issued its policy of insurance naming the Defendant, Mrs. Gutierrez, as named insured thereunder, and on May 26, 1964, Mrs. Gutierrez was in the insured automobile while it was being driven by Lombardo at which time the automobile struck a child pedestrian, the deceased son of the Defendants, Mr. and Mrs. Dorr (Amended Complaint, Paragraph VI, TR 6). Thereafter, Mr. Dorr, as the surviving father of his son, brought an action against Lombardo and Mrs. Gutierrez and recovered a judgment against them in the amount of \$20,000.00 to-

gether with interest and costs. (See the Motion for Summary Judgment of the Dorrs, together with the affidavit of Kenneth Rosengren attached thereto, to which is attached a copy of the judgment in Civil Action No. 163317 of the Maricopa County Superior Court, TR 19.)

Lombardo was also insured under liability policy issued by the Defendant Badger at the time of the accident (Paragraph VII, Plaintiff's Amended Complaint, TR 6), and the Amended Complaint seeks to determine the respective obligations as between the Defendant Badger and the Plaintiff with respect to the coverage afforded to the Defendant Lombardo as a result of the motor vehicle accident. (See Paragraph 4 of the prayer to the Amended Complaint, TR 8.)

The Motion for Summary Judgment was predicated upon the concept that under Arizona Revised Statutes 28-1170 A.R.S., Subsection F applied to all motor vehicle liability policies in the State of Arizona and as a result thereof, the liability of all insurance companies became absolute at the time that an accident occurred with respect to damage arising out of the accident, regardless of the fraud perpetrated by the insured initially in procuring the liability insurance policy (TR 16). With this concept, the Court agreed and entered judgment against the Plaintiff, Allstate.

SPECIFICATION OF ERRORS

The court erred in granting the motion for summary judgment of the Defendants Dorr for the following reasons:

(a) The court was required to accept as true the pleadings of Allstate supported by affidavits that the policy of insurance issued to Gutierrez was void for fraudulent misrepresentations in the application for insurance.

(b) The rights of the Defendants Dorr against Allstate are no greater than the rights of an insured and, thus, the void policy affords no coverage to the Defendants Dorr.

(c) The action of the court in enforcing coverage in the face of fraudulent misrepresentations by the Defendant Gutierrez is an deprivation of liberty and property without due process of law in violation of the 14th Amendment to the U. S. Constitution and in violation of Article II, Section 4, of the Constitution of the State of Arizona.

ARGUMENT OF THE CASE

Summary of Argument

1. The Federal and Arizona State Constitutions protect the right to contract under the due process clause.

2. Substantive due process prohibits the State of Arizona from interfering with the right of contract except in exercise of the police power to correct some actual or manifest evil.

3. The Financial Responsibility Act of Arizona is an exercise of the police power for the purposes enumerated by the Arizona Supreme Court.

4. The right to avoid a contract induced by fraudulent misrepresentations is a part of the right to contract protected by the due process clause.

5. Arizona law recognizes the right to avoid an insurance contract for misrepresentation of a material fact, if the insurance company *might have been* influenced by truth.

6. The application of the Financial Responsibility Act so as to prevent any insurer from avoiding any policy after loss has occurred regardless of what fraudulent misrepresentations are made is an unconstitutional application of the Act in that it deprives the insurer of substantive due process.

Both the 14th Amendment to the United States Constitution and Article II, Section 4 of the Constitution of Arizona provide that no persons shall be deprived of life, liberty or property without due process of law. Courts are most frequently called upon to review the procedural aspects of the due process clause whereby notice and an opportunity to be heard and to defend are the essential elements. (For example, see *Phoenix Metals Corp. v. Roth*, 79 Ariz. 106, 284 P.2d 645.)

Substantive due process as opposed to procedural due process has been recognized by the State of Arizona as well as the Federal Courts. *Valley National Bank of Phoenix v. Glover*, 62 Ariz. 538, 159 P.2d 292. The Arizona Supreme Court defined substantive due process as follows at 159 P.2d 298:

“Due process when applied to substantive rights, is interpreted to mean that the state is without right to deprive a person of life, liberty or property by an act that has no reasonable relation to any proper governmental purpose, or which is so far beyond the necessity of the case as to be an arbitrary exercise of governmental powers.”

The due process clause does not have the effect of prohibiting the State from enacting police measures under the police power appropriate to correct some actual or manifest evil. Such a regulation must be reasonably necessary to secure the health, safety, good order, comfort or general welfare of the community, *Atlantic Coastline v. Goldsboro*, 232 U.S. 548, but the method employed by the State must bear a real and substantial relationship to a public end. *Liggett Co. v. Baldridge*, 278 U.S. 105. These concepts have been defined in the following terms:

“In determining whether legislation is violative of constitutional restraints, the courts will confine them-

selves to the question, not of legislative policy, but of legislative power. The law must not be arbitrary, unreasonable or patently beyond the necessities of the case. The legislature may not under the guise of protecting public interests arbitrarily interfere with private business or impose unnecessary restriction upon lawful occupations. If the law prohibits that which is harmless in itself or if it is unreasonable and purely arbitrary, or requires that to be done which does not tend to promote the health, comfort morality, safety or welfare of society, it is an unauthorized exercise of power."

Departments of Financial Institutions v. Holt, (Ind.)
108 N.E.2d 629 at 634.

South Dakota described the rule in the following manner:

"Nevertheless, due process still requires that any exercise of the police power be reasonable, . . . and the regulatory means adopted by the legislature must bear a real and substantial relation to some actual or manifest evil, . . . and cannot be unreasonable, arbitrary or capricious. The determination of such issues is a judicial function and when a measure is found to be in violation of our fundamental law it is void."

To the same effect, see *Treigle v. Acme Homestead Assn.*, 297 U.S. 189, and *Smith v. Texas*, 233 U.S. 630.

Although the term "person" is used in both the 14th Amendment to the United States Constitution and in the Arizona Constitution, nevertheless, such term also applies to a corporation such as Allstate. *Covington v. Sanford*, 164 U.S. 592.

Thus, we must turn to the action of the State of Arizona and determine whether the District Court in following the rules layed down by the State of Arizona Supreme Court violated the Federal Constitution.

The passage of the Financial Responsibility Act by the legislature of the State of Arizona was an exercise of the police power. *Schechter v. Killingsworth*, 93 Ariz. 273, 380 P.2d 136. In *Jenkins v. Mayflower*, 93 Ariz. 287, 380 P.2d 145, the Arizona Supreme Court considered that portion of the Financial Responsibility Act of the State of Arizona set forth in the Statute 28-1170 A.R.S. (See Appendix A for the entire text of this statute.) In that case the Arizona Supreme Court held that Subsection B of the statute required all automobile liability policies to contain a provision commonly referred to as the "omnibus clause". By requiring such a provision be included in all automobile liability policies, the Supreme Court so applied the statute as to require insurance coverage be afforded any person driving a motor vehicle with the permission of the named insured under the automobile liability policy.

Subsequently, the Arizona Supreme Court in the case of *Sandoval v. Chenoweth*, 102 Ariz. 241, 428 P.2d 98, held:

"Under the rule expressed in *Mayflower*, the provisions of the Financial Responsibility law are applicable to the facts of the instant case whether or not the policy would be technically classified as a 'certified' policy. A.R.S. Sec. 28-1179 expressly states as follows:

'F. Every motor vehicle liability policy shall be subject to the following provisions which need not be contained therein :

"1. The liability of the insurance carrier with respect to the insurance required by this chapter shall become absolute when injury or damage covered by the motor vehicle liability policy occurs. The policy may not be cancelled or annulled as to such liability by an agreement between the insurance carrier and the insured after the occurrence of the injury or damage, and no statement made by the insured or on

his behalf *and no violation of the policy shall defeat or void the policy.*" (Emphasis added by the court.) 42S P.2d 101.

The District Court applied that same provision of the statute in order to hold as a matter of law that Allstate could not secure a determination that the policy of insurance was void *ab initio* by virtue of the fraudulent misrepresentations of the applicant Gutierrez.

It would seem unquestioned that as an incident to the right to contract without unreasonable restraint included the right to freely contract and to avoid those contracts not freely made (that is, made only by virtue of the inducing fraudulent misrepresentations).

A similar concept is the concept that the liberty of contract involves as one of its essential attributes the right to terminate a contract subject only to civil liability for unwarranted termination. This concept has been enumerated on many occasions. 16 AmJur 2d 706, *Constitution of Law*, Sec. 373. The concept has been frequently applied in connection with statutes which prohibit employers from attaching conditions to employment. 68 A.L.R. 1269.

It is not surprising that the courts would so interpret the provisions of the Constitution inasmuch as the right to contract freely without unreasonable restraint is considered one of the fundamental liberties of the individual protected by the 14th Amendment. *U.S. v. Seven Oaks Dairy Co.*, 10 F.Supp. 995 (D.C. Mass. 1935). The right of liberty of contract was a concept originally advanced by Justices Bradley and Field in the *Slaughterhouse* cases, 16 Wall 36 (1833). Such concept was elevated to the status of an accepted doctrine in 1897 in *Allgeyer v. Louisiana*, 165 U.S. 578. Freedom from interference is the general rule and restraint upon the liberty of contract is the exception which

can be justified only by exceptional circumstances. *Wolff Packing Co. v. Court of Industrial Relations*, 262 U.S. 522.

In *Conold v. Stern*, (Ohio) 35 N.E. 2d 133, the Supreme Court of Ohio held that to deprive the insurance company of a provision of the insurance policy would be to violate the due process clause. The exact language doubly applicable here is as follows :

“The conditions and limitations of the policy are enforceable, not only against the insured but against all persons who seek relief under it. Otherwise, the statute would violate the due process clause of the constitution.”

One of the very questions falsely answered by the applicant Gutierrez in the instant case has been held to give the insurance company the right to declare the policy void. The Arizona Supreme Court held as follows :

“ . . . When an insurance company has asked of an applicant whether he has previously been rejected for insurance, a false answer is sufficient to authorize the company to declare the policy void without the necessity of proving whether it would have rejected the application if it had knowledge of that fact.”

First Benefit Society v. Fisk, 55 Ariz. 290, 101 P.2d 205, at 207.

See also *Illinois Bankers Life Assn. v. Theodore*, 44 Ariz. 160, 34 P.2d 423; *American National Ins. Co. v. Caldwell*, 70 Ariz. 78, 216 P.2d 413; *Modern Woodmen of America v. Stevens*, 70 Ariz. 232, 219 P.2d 322; *Mutual Life Ins. Co. of N.Y. v. Morairty*, 178 F.2d 470; *Byrnes v. Mutual Life Ins. Co. of N.Y.*, 217 F.2d 497.

When a state invokes the police power as a justification for infringing upon 14th Amendment rights, the action of the State will be upheld only when that action bears a real

and substantial relation to the end sought to be accomplished. *Liggett Co. v. Baldrige*, *supra*, at 73 L.Ed. 208; *Department of Financial Institutions v. Holt*, *supra*. The purpose of the Arizona Financial Responsibility Act is described in *Schechter v. Killingsworth*, *supra*, at 380 P.2d 140 as follows:

“The Financial Responsibility Act has for its principal purpose the protection of the public using the highways from financial hardship which may result from the use of automobiles by financially irresponsible persons. It accomplishes the objective by requiring proof of financial responsibility by those involved in an accident, either by a showing of insurance which covers deposit of cash or securities. It may, as incidental purposes and effects, because of the threat of loss of driving rights following an uninsured accident, (1) encourage operators of motor vehicles to obtain liability insurance, and (2) encourage drivers to drive more carefully. Because the uninsured motorist can avoid the adverse effects of the statute without obtaining insurance, and without improving his driving practices (i.e. by putting up security—here \$425.00—or by obtaining a release from the injured party, or an agreement for payment of damages in installments) we cannot consider either the encouragement to obtain insurance or the improvement of safety conditions on the highway to be primary objectives of this law.”

It seems clear that depriving an insurance company of the right to declare void a contract induced by fraud is not a reasonable method of accomplishing those ends described.

The fact that the claim being asserted against the insurance company here is asserted by one other than the applicant who made the false statements does not affect the right of the insurance company to avoid coverage, for the rights of others claiming against or under the insured

Gutierrez can rise no higher than the rights of Gutierrez herself. *Conold v. Stern, supra; State Farm Mut. v. Butler*, (Va.) 125 S.E.2d 823 at 827. This court in construing Arizona law has said much the same thing in *Byrnes v. Mutual Life Ins. Co.*, 217 F.2d 497, at 502, wherein it was said:

"This court, in the Widow's case and the Supreme Court of Arizona in the cases cited, have applied this principal and have held that the *insured and those who claim under him* are found by his representations and that the Company had the right to rely on them and that knowledge as to the falsity of some of them does not invalidate the policy." (Emphasis the court's.)

It would seem to go without citing authority that the District Court is not justified in violating the due process clause of the Constitution notwithstanding that the District Court was apparently following the dictates of the Arizona Supreme Court in so doing.

CONCLUSION

It is respectfully submitted that the judgment in the above entitled action must be reversed.

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I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

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APPENDIX A

§ 28-1170. "Motor vehicle liability policy" defined

A. A "motor vehicle liability policy" as the term is used in this chapter means an owner's or an operator's policy of liability insurance, certified as provided in § 28-1168 or § 28-1169 as proof of financial responsibility, and issued, except as otherwise provided in § 28-1169, by an insurance carrier duly authorized to transact business in this state, to or for the benefit of the person named therein as insured.

B. The owner's policy of liability insurance must comply with the following requirements:

1. It shall designate by explicit description or by appropriate reference all motor vehicles with respect to which coverage is thereby to be granted.

2. It shall insure the person named therein and any other person, as insured, using the motor vehicle or motor vehicles with the express or implied permission of the named insured, against loss from the liability imposed by law for damages arising out of the ownership, maintenance or use of the motor vehicle or motor vehicles within the United States or the Dominion of Canada, subject to limits exclusive of interest and costs, with respect to each motor vehicle as follows:

- (a) Ten thousand dollars because of bodily injury to or death of one person in any one accident.

- (b) Subject to the limit for one person, twenty thousand dollars because of bodily injury to or death of two or more persons in any one accident.

- (c) Five thousand dollars because of injury to or destruction of property of others in any one accident.

C. The operator's policy of liability insurance shall insure the person named as insured therein against loss from the liability imposed upon him by law for damages

arising out of the use by him of any motor vehicle not owned by him, within the same territorial limits and subject to the same limits of liability as set forth in subsection B of this section with respect to an owner's policy of liability insurance.

D. The motor vehicle liability policy shall state the name and address of the named insured, the coverage afforded by the policy, the premium charged therefor, the policy period and the limits of liability, and shall contain an agreement or be endorsed that insurance is provided thereunder in accordance with the coverage defined in this chapter as respects bodily injury and death or property damage, or both, and is subject to all the provisions of this chapter.

E. The motor vehicle liability policy need not insure liability under any workmen's compensation law nor liability on account of bodily injury to or death of an employee of the insured while engaged in the employment, other than domestic, of the insured, or while engaged in the operation, maintenance or repair of the motor vehicle nor liability for damage to property owned by, rented to, in charge of, or transported by the insured.

F. Every motor vehicle liability policy shall be subject to the following provisions which need not be contained therein :

1. The liability of the insurance carrier with respect to the insurance required by this chapter shall become absolute when injury or damage covered by the motor vehicle liability policy occurs. The policy may not be cancelled or annulled as to such liability by an agreement between the insurance carrier and the insured after the occurrence of the injury or damage, and no statement made by the insured or on his behalf and no violation of the policy shall defeat or void the policy.

2. The satisfaction by the insured of a judgment for the injury or damage shall not be a condition precedent to the

right or duty of the insurance carrier to make payment on account of the injury or damage.

3. The insurance carrier shall have the right to settle any claim covered by the policy, and if the settlement is made in good faith, the amount thereof shall be deductible from the limits of liability specified in paragraph 2 of subsection B of this section.

4. The policy, the written application therefor, if any, and any rider or endorsement which does not conflict with the provisions of the chapter shall constitute the entire contract between the parties.

G. A policy which grants the coverage required for a motor vehicle liability policy may also grant lawful coverage in excess of or in addition to the coverage specified for a motor vehicle liability policy and the excess or additional coverage shall not be subject to the provisions of this chapter. With respect to a policy which grants the excess or additional coverage the term "motor vehicle liability policy" shall apply only to that part of the coverage which is required by this section.

H. A motor vehicle liability policy may provide that the insured shall reimburse the insurance carrier for any payment the insurance carrier would not have been obligated to make under the terms of the policy except for the provisions of this chapter.

I. A motor vehicle liability policy may provide for the prorating of the insurance thereunder with other valid and collectible insurance.

J. The requirements for a motor vehicle liability policy may be fulfilled by the policies of one or more insurance carriers which policies together meet the requirements.

K. A binder issued pending the issuance of a motor vehicle liability policy shall be deemed to fulfill the requirements for such a policy. As amended Laws 1961, Ch. 94, § 4.

